

Office of the Inspector General

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Allegation of a Violation of the State Procurement Code and Other Issues Related to a Statewide Term Contract Involving the Department of Revenue and the Department of Health and Environmental Control

I. Executive Summary

A complainant alleged the Department of Revenue (DOR) violated the South Carolina Procurement Code by inappropriately having an existing subcontractor, SAS, purchase the “Experian Identity Proofing Solution” software service under the purchase authority of a statewide term contract DOR used to procure the “SAS Fraud Framework.” It was alleged this transaction was executed to avoid a competitive procurement where the complainant’s client could have competed along with as many as 10 other vendors. A number of convoluting factors gave rise to the complainant’s suspicions, but a review of the transaction determined the allegation to be unfounded. However, during the review of this Experian transaction, it was determined the SAS Fraud Framework was inadvertently, as well as inappropriately, placed on the statewide term contract.

The statewide term contract used by DOR to purchase the SAS Fraud Framework originated in 2014 as a DHEC request for proposals (RFP) for a Master Data Management (MDM) Solution, which pertained to agency data governance. During the routine vendor questioning period after the RFP was published, a vendor asked if the solicitation could be expanded to a statewide term contract to allow other state agencies to acquire the MDM solution. As a result, the DHEC RFP was amended to change the solicitation from a solution for DHEC to a statewide term contract. Almost every interviewee viewed this conversion of an ongoing DHEC RFP into a statewide term contract as unusual.

Four proposals were received from vendors, and a proposal from Executive Information System LLC (EIS) was ranked the highest by the RFP evaluation panel. EIS was the public sector marketing entity for SAS, with SAS appearing as a subcontractor in EIS’s proposal. The key aspect of the RFP impacting the SAS Fraud Framework pertained to a clause asking vendors to “identify any additional services that may be offered to the State.” The clause further stated the additional services will not be part of the evaluation, but will be for informational purposes only and could be part of the contract at the sole discretion of the State (DHEC). Four additional services were proposed by EIS: an on-site Program Director to assist DHEC in the implementation of the MDM solution at \$250 per hour; a Disaster Recovery and Redundant Systems for electronic data at \$480,000 per year; the SAS Fraud Framework to uncover suspicious behavior and prevent fraudulent transactions for a \$1,500,000 license fee per agency plus implementation charges; and a SAS Prescription Drug Monitoring Solution at \$900,000 for software and implementation.

After EIS was ranked the highest by the evaluation panel, the Materials Management Office’s (MMO) Procurement Manager, along with DHEC’s Procurement Director and Office of General Counsel, entered into negotiations with EIS to attempt to finalize a contract. The state was required by law to, “negotiate the business proposal from the highest ranked offeror and seek significant savings while maintaining the offer as it was proposed.” The Record of Negotiations (RON) did not reflect any negotiations pertaining to the four “additional services” offered. Based on interviews of the MMO Procurement Manager and the DHEC Procurement Director, there was no indication any of the additional services were negotiated, nor did the State’s negotiation team assure the technical requirements and value of these four additional services had been assessed. These additional services were inadvertently added to the statewide contract without competition as they had not been included in the specifications requiring all vendors to propose similar services.

From a DHEC perspective, these four “additional services” could be accepted or rejected having little consequence. However, the negotiated contract turned into a statewide contract with a seven year term, so these four “additional services” essentially bound every other state agency to use these services at the stated price, absent unique circumstances. This gave EIS an exclusive on selling these services to other state agencies over the seven year contract, yet these same agencies would be unaware the price and technical requirements were never competed or evaluated as required for a statewide term contract. The intent of a statewide contract is to

make available to multiple agencies a product or service meeting agencies' common needs, likely at lower prices by competing the greater combined purchase volume, as well as saving agencies the administrative effort of conducting separate procurements.

Other issues determined during the review of both DOR's Experian purchase and DHEC's MDM purchase included:

- Converting the MDM Solution for agency data governance to a statewide term contract was questionable in that the compressed time frame potentially limited competition and prevented a broader, more technically qualified evaluation panel's involvement to commit all other state agencies to this statewide term contract;
- DOR used questionable business judgment in agreeing to pay EIS in full for the SAS Fraud Framework within 30 days of contract signing before successful implementation with a seven month timeline, due to DOR's need to expend funds that could not be carried forward to another fiscal year; and
- DHEC initiated the MDM project on 1/2/2015 by issuing a purchase order totaling \$3,199,247 without adequate funding to complete the project. After additional funds were not approved by the General Assembly and a reevaluation of its priorities, DHEC cancelled the project. \$1,599,624 had been expended prior to cancellation, much of which amounted to unrecoverable sunk costs.

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Appendices A – DHEC Request for Proposal – October 10, 2014

(Internet Link: http://oig.sc.gov/Documents/DHEC_RFP_Oct_2014.pdf)

Appendices B – Amendment 1 to the Request for Proposal – October 31, 2014

(Internet Link: http://oig.sc.gov/Documents/Amendment_1_to_RFP.pdf)

Appendices C – EIS Proposal – November 12, 2014

(Internet Link: http://oig.sc.gov/Documents/EIS-SAS_Proposal.pdf)

Appendices D – Record of Negotiations – December 22, 2014

(Internet Link: http://oig.sc.gov/Documents/Record_of_Negotiations.pdf)

II. Background

A. Predicate

A complainant alleged the Department of Revenue (DOR) violated the South Carolina Procurement Code by inappropriately having an existing subcontractor, SAS, purchase a software service known as the “Experian Identity Proofing Solution” under the purchase authority of a statewide term contract DOR used to procure the “SAS Fraud Framework.” This transaction was allegedly executed to avoid a competitive procurement where the complainant’s client could have competed along with as many as 10 other vendors. The complainant was only able to piece this allegation together from heavily redacted documents obtained from DOR after a Freedom of Information Act (FOIA) request.

B. Scope & Objectives

This review’s scope and objectives were:

- Examine the DOR’s procurement of the Experian Identity Proofing Solution to determine if there were State Procurement Code violations, principally the inappropriate use of an existing statewide contract to make a non-competitive purchase for DOR; and
- During the review of DOR’s Experian Identity Proofing Solution procurement, a second objective was established to determine how the SAS Fraud Framework was placed on the statewide term contract.

Reviews by the SIG are conducted in accordance with professional standards set forth by the Association of Inspectors General, often referred to as the “Green Book.”

III. DOR Purchase of the “Experian Identity Proofing Solution”

On 5/15/2015, DOR issued a purchase order for the “SAS Fraud Framework” to Executive Information System LLC (EIS), which provided this product under its broader statewide term contract emphasizing agency data governance known as the “Master Data Management Solution (MDM).” The purchase order totaled \$3,870,000 and included three items: SAS Fraud Framework license (\$1,935,000, including hosting); Processing Historical Data (\$835,000); and Test Ready System delivery (\$1,100,000). The purchase order called for a delivery date of 6/15/2015. The vendor invoiced all three items on 5/31/2015 and the invoice was paid on 6/25/2015, despite an estimated seven month implementation timeline. Subsequently, DOR issued a second purchase order, dated 7/24/2015, totaling \$480,000 for “Support Services for SAS Framework,” which was paid on 8/7/2015.

A key aspect of the complainant’s allegation was an unusual proposed contract change order by DOR to the state’s Materials Management office (MMO), which managed this statewide term contract. The complainant alleged this change order was designed to circumvent the State Procurement Code to avoid competing the Experian Identity Proofing Solution purchase. The proposed change order, in short, allowed an agency’s scope of work with the statewide contract vendor, EIS, to take precedence over the original statewide contract terms. Obviously, MMO rejected DOR’s proposed change order due to the inappropriateness of permitting any state

agency to override the terms of the existing statewide contract. Through interview, DOR denied the change order's purpose was to circumvent a competitive procurement of the Experian Identity Proofing Solution. Rather, it was to assure DOR's stringent information security requirements would not be impinged by any aspect of the original statewide contract.

The complainant was associated with Lexis-Nexis (LN), a vendor DOR had contracted with in prior years to assist in the detection of fraudulent income tax refund filings. In early 2015, DOR was negotiating with LN to again utilize their services. In May 2015, these negotiations turned to using the LN service in conjunction with the fraud detection analytics provided by the SAS Fraud Framework. Based on DOR's May 2015, Scope of Work with EIS for the SAS Fraud Framework, DOR was to contract directly with LN for the identity verification of tax return filers. DOR was to forward those verification results to SAS along with internal DOR data for SAS to use in their process of determining potential fraud. A DOR official characterized the arrangement as "a multi-vendor process that would consider all aspects and information to stop as much fraud as possible by utilizing identity data from LN and financial analytics from SAS."

Negotiations with LN proceeded into June 2015, when DOR abandoned its effort to use LN's service after LN did not offer an alternative without their "Knowledge Quiz" component. The "Knowledge Quiz" uses "out-of-the-wallet" questions to verify identity, and its use under LN's prior contract had been problematic for DOR. In addition, LN only offered a performance-based contract with fees determined as a percentage of fraudulent return filings. DOR and LN had been unable to agree on which filings were actually fraudulent during their prior contract.

After abandoning the use of LN's service, DOR asked SAS if they could simply buy identity data from LN or another vendor and incorporate the identity verification requirement into their process. SAS agreed and Experian was ultimately selected to provide the identity data. Since SAS assumed responsibility for identity verification and the process was hosted by SAS, it was logical for SAS to acquire the identity data directly from Experian as a raw material for their process. DOR, EIS (SAS prime subcontractor), and Experian entered into agreements for SAS to directly purchase the Experian data with SAS performing the identity verification in addition to their analytics to identify fraudulent tax refund filings.

From the perspective of the complainant, it appeared on the surface DOR had indeed acquired a service without competition by having a subcontractor on an existing contract purchase the service. Adding to that appearance was DOR's heavy redaction of complainant's FOIA requested documents to fully understand the transactions. Additionally, even though DOR made the decision to abandon utilizing LN's service in mid-June, the complainant stated LN was not notified until early August and was not given a comprehensive reason for the decision. However, given the change in the process with SAS having the final responsibility to deliver an effective identity verification capability, it was logical for SAS to purchase the Experian data directly.

Even though the allegation was unfounded, it was noted DOR paid in full for the SAS Fraud Framework within 30 days of invoicing despite the fact the majority of the cost was in hourly fees for development and implementation of the solution over an estimated seven month timeline. This early payment was in contrast to EIS/SAS' agreement, as shown in the Record of Negotiations, which required payment of the first year's cost of the Data Governance and MDM solution be made in quarterly installments. In the final analysis, EIS did not

require advance payment. DOR paid prior to accepting a successful implementation due to DOR's need to expend funds by 6/30/2015, which DOR stated could not be carried forward to another fiscal year. Paying in full before successful implementation was not a generally accepted prudent business practice, particularly in technology contracts which have a high failure rate.

During the review of this DOR contract, questions were raised as to how the SAS Fraud Framework was placed on the statewide contract in a non-competitive manner during the negotiation of a statewide term contract designed for agency data governance.

IV. DHEC Purchase of the Master Data Management Solution

The statewide term contract used by DOR to purchase the SAS Fraud Framework originated in 2014 as a DHEC procurement for a Master Data Management (MDM) Solution, which pertained to managing agency-wide data within a governance framework. The RFP process was managed by MMO since the proposed solution was expected to exceed DHEC's authorized technology procurement threshold of \$225,000. The RFP was published on 10/10/2014 (*see Appendix A*). The RFP process included a pre-proposal conference on 10/22/2014 with a proposal submission deadline of 11/10/2014.

At the pre-proposal conference, a vendor asked if the solicitation could be expanded to allow other state agencies to acquire the MDM solution. MMO's published response was, "after discussion with DHEC and other State officials it has been determined that this solicitation will result in a contract being awarded as a Statewide Term Contract that will allow other agencies the ability to utilize the services for Data Governance Framework and Master Data Management Solution." As a result, MMO issued Amendment "1" to the solicitation on 10/31/2014, changing the solicitation from a solution for DHEC to a statewide term contract (*see Appendix B*). In addition, the amendment addressed some of the 122 pre-proposal vendor questions and extended the proposal deadline by four days to 11/14/2014. Almost every interviewee viewed this conversion of an ongoing DHEC RFP into a statewide term contract after publishing an RFP as unusual.

Four proposals were received from vendors. EIS's proposal was ranked the highest by the RFP evaluation panel (*see Appendix C*). EIS acted as the contractor for SAS in the public sector utilizing its sales force, business development, and contract management capabilities. The key aspect of the RFP impacting the SAS Fraud Framework pertained to a clause asking vendors to "identify any additional services that may be offered to the State." The clause further stated the additional services will not be part of the evaluation, but will be for informational purposes only and could be part of the contract at the sole discretion of the State (DHEC). EIS proposed the following four additional services (*see Appendix C, page 87*):

- An on-site Program Director to assist DHEC in the implementation of the MDM solution for \$250 per hour;
- Disaster Recovery and Redundant Systems – A number of cloud-based services including disaster recovery and hosting of DHEC's data and applications in SAS's data center for \$480,000 per year;

- The SAS Fraud Framework – an application to uncover suspicious behavior and prevent fraudulent transactions. The proposal noted DHEC had an existing hosted implementation of the SAS Fraud Framework licensed for risk-scoring of health facilities due for inspection. This additional service would expand the license to include more modules to help DHEC address a wide range of issues for a \$1,500,000 license fee plus implementation charges; and
- SAS' Prescription Drug Monitoring Solution – A module of the SAS Fraud Framework license to enable DHEC to monitor prescription drug use for \$900,000 for software and implementation.

After EIS's proposal was ranked the highest by the evaluation panel, the MMO Procurement Manager, along with DHEC's Procurement Director and Office of General Counsel, entered into negotiations with EIS to attempt to finalize a contract. The State was required by law to, "negotiate the business proposal from the highest ranked offeror and seek significant savings while maintaining the offer as it was proposed." The Record of Negotiation (RON) did not reflect any negotiations pertaining to the four "additional services" offered (*see Appendix D*). Based on interviews of the MMO Procurement Manager and the DHEC Procurement Director, there was no indication any of the additional services were negotiated. The MMO Procurement Manager had no recollection of negotiating the "additional services," but assumed DHEC's subject matter experts may have done so. An interview of the DHEC Procurement Director determined there were no negotiations on the price of the "additional services," nor was he aware of any technical assessment of the "services" or prices offered.

These additional services were added to the contract without competition, as they were not specifically requested of all vendors in the RFP. Both the MMO Procurement Manager and the DHEC Procurement Director, in hindsight, viewed these additional services as predominantly atypical in that, other than the on-site program director, the other three appeared to be standalone products. SAS advised it was just following the RFP request for other services, which ended up in the finalized contract. Based on the evidence, the additional services were inadvertently added to the statewide contract.

As an aside, IT disaster recovery planning and preparation has been a critical concern related to the state's information security initiative, and was underscored by Legislative Budget Proviso 117.131 for FY 2014-15, requiring a study to develop recommendations for a statewide IT disaster recovery plan. As a result, a number of agencies have implemented disaster recovery initiatives or have them under consideration. However, agencies may not be aware of the existing statewide term contract, which includes the SAS Disaster Recovery and Redundant Systems additional service, because it cannot be found in the term contract listing. In addition, senior staff members of the state's Division of Information Security were unaware of its existence.

From a DHEC perspective, these four "additional services" could be accepted or rejected having little consequence. However, their inclusion on the statewide term contract essentially bound every other State agency to use these services at the stated prices, absent unique circumstances. This gave EIS an exclusive to sell these additional services to other State agencies over the seven year term of the contract, and those agencies would be unaware the price and technical requirements were never competed or evaluated as required in a public procurement process. The intent of a statewide contract was to make available to multiple agencies a product or service meeting agencies' common needs, likely at lower prices by competing the greater combined purchase volume, and saving agencies the administrative effort of conducting separate procurements.

DHEC issued a purchase order on 1/2/2015 for the MDM Solution. The purchase order totaled \$ 3,199,247, however DHEC did not have funding available to complete the project. Additional funds were requested in DHEC's FY 2015-16 budget request, but were not approved by the General Assembly. Without complete funding, DHEC reevaluated its priorities and cancelled the project on 7/29/2015 after making two quarterly payments totaling \$1,599,624. None of the additional services were included in DHEC's PO, and a review of purchases under this statewide term contract showed no other State agencies, other than DHEC and DOR, have made purchases for any items under the contract.

A secondary issue pertained to the amendment of the original DHEC RFP after it was published. The DHEC RFP was amended three weeks after it was published converting it from an RFP solely for DHEC to an RFP to create a statewide term contract making the MDM Solution available to all State agencies. This change after the requirements and specifications were published to potential vendors, appeared unusual and uncharacteristic of the process to develop a statewide term contract. Since a primary purpose of statewide term contracts was the consolidation of multiple agencies' needs to achieve the most optimal vendor offerings, logic would dictate such a process should include a careful assessment of those needs in advance, with the assessment communicated to potential vendors in the RFP. Apparently, no assessment took place and even though the amendment extended the proposal deadline four days, the revised deadline was only two weeks from the date the amendment was published. At that point it was unlikely any vendors involved in the process of developing proposals had time to assess statewide needs, and it would likely have been too little time for other vendors, attracted by the potential larger volume, to prepare offers.

V. DOR Purchase of the SAS Fraud Framework Solution

DOR staff involved in the purchase of the SAS Fraud Framework first became aware of the product in April 2015 when SAS demonstrated their product for DOR. It was at that time DOR staff also became aware this product was on the statewide term contract. DOR vetted the product by analyzing its features. The main benefit was SAS' ability to quickly arrive at a conclusion on a refund request where in some cases it had taken DOR until June of each year to make a determination. The delay was due to DOR's reliance on the employer's copy of the W2 to resolve questionable refund requests, which could not be completely loaded in DOR's 30 plus year old mainframe computer system until June of each year. The SAS Fraud Framework analytics also determined variances from prior return filings, something DOR could not do with their old system.

The SAS Fraud Framework appeared to meet DOR's needs and it was quickly obtained since it was on statewide contract. However, the SAS Fraud Framework being on statewide contract precluded DOR from exploring other potential vendors' products and conducting a competitive procurement process to ensure it received a product best suited to its needs at the best price.

VI. Findings & Recommendations

Finding #1: The allegation DOR violated the State's Procurement Code by circumventing a competitive procurement of the Experian Identity Proofing Solution was unfounded; however, poor communications between DOR and Lexis Nexis contributed to the complainant's allegation.

Finding #2: Additional services proposed by the successful vendor to the MDM Solution RFP were allowed to become offerings on a statewide term contract without competition, evaluation, negotiation, or proper vetting, which required other State agencies, absent compelling reasons, to exclusively use these products.

Recommendation #2: The Procurement Services Division, State Fiscal Accountability Authority, should consider removing the SAS Fraud Framework, Disaster Recovery and Redundant Systems, and Prescription Drug Monitoring Solution from the statewide term contract.

Finding #3: Converting the MDM Solution for agency data governance to a statewide contract after publication of an RFP and only extending the RFP deadline four days unnecessarily manufactured a compressed response time frame potentially limiting competition and preventing a broader, more technically qualified evaluation panel's involvement to commit all other State agencies to this statewide contract decided solely by DHEC employees.

Recommendation #3: The Procurement Services Division, State Fiscal Accountability Authority should consider establishing a policy for converting an existing RFP into a statewide term contract if planned to be a recurring practice.

Finding #4: DOR used questionable business judgment in agreeing to pay a contractor in full within 30 days of contract signing for a contracted software solution totaling \$3,870,000 of which \$2,370,000 of the costs represented consulting services by the contractor for implementation of the solution with an estimated timeline of seven months, particularly with a technology contract, which have a high rate of failures.

Finding #5: DHEC initiated the MDM project without adequate funding to complete the project and ultimately cancelled the project due to a lack of funding and a reevaluation of priorities after expending \$1,599,624, much of which were unrecoverable sunk costs.

ADMINISTRATIVE NOTE:

DOR did not provide any comments and did not object to the report's findings and recommendations. DHEC provided informal comments, which were factored into the final report, and did not object to the report's findings and recommendations. The Division of Procurement Services provided a response located at the following link: <http://oig.sc.gov/Documents/Division-of-Procurement-Services-Response.pdf>